

Stakeholders' Reactions to ESG Scores and Political Connections: Evidence from Tobin's Q and Stock Performance

Nindya Farah Dwi Puspitasari^{1*}, Sri Indah Nikensari², Pesi Suryani³

^{1,3}Faculty of Economics and Business, Universitas Terbuka, Tangerang Selatan, Indonesia

²Faculty of Economics and Business, Universitas Negeri Jakarta, Jakarta, Indonesia

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ABSTRACT

This study seeks to determine how environmental, social and governance (ESG) scores and corporate political connections jointly shape stakeholder reactions, captured through firm-level valuation (Tobin's Q) and stock returns, among Indonesian listed companies. Using firm-level panel data for listed companies over 2020-2023, this quantitative study applies Generalized Least Squares estimation in Stata, and augments the analysis with contextual information drawn from peer-reviewed journals and reputable online sources. Stronger ESG scores raise firm valuations (Tobin's Q) without enhancing total stock returns, whereas political connections lower Tobin's Q by about 0.17 yet deliver an average excess return of roughly 0.69 percentage points. The evidence indicates that sustainability credentials and political affiliations influence performance in mutually reinforcing yet distinct ways: stronger ESG scores are associated with durable gains in enterprise value, whereas political connections translate into only short-lived share-price uplifts. Consequently, the findings encourage executives to invest in substantive ESG improvements as a foundation for lasting value creation, while cautioning regulators that the abnormal returns enjoyed by politically connected firms may stem from rent-seeking rather than genuine efficiency.

1. Introduction

Financial statements serve as the primary vehicle through which a firm conveys its financial performance to stakeholders for decision-making purposes. Research by Biehl et al. (2024) indicates that the higher the quality of those statements, the more efficiently the reporting firm allocates its resources. However, many observers now contend that traditional financial data alone no longer fully satisfies users' information requirements. They also demand for non-financial information in decision making.

Within the continually developing framework of the International Financial Reporting Standards (IFRS), sustainability information is treated as an integral component of financial reporting rather than a peripheral add-on. IFRS S1 obliges companies to report any sustainability risks and opportunities that can reasonably be expected to affect their future cash flows, financing

prospects, or cost of capital over the short, medium, and long term, thereby supplying investors with information that is truly decision-relevant (International Sustainability Standards Board (ISSB), 2023a). Moreover, IFRS S2 complements this overarching standard by prescribing granular reporting on both physical and transition climate risks and the associated opportunities, including the time horizons over which such effects may materialise. These climate-specific disclosures are designed to enhance comparability and enable users of general-purpose financial statements to allocate resources more efficiently in response to climate-related uncertainties (International Sustainability Standards Board (ISSB), 2023b).

A widely used framework for assessing corporate sustainability is the Environmental, Social, and Governance (ESG), which now serves both as a central criterion in corporate and investment decision-making (KEY ESG, 2025), and as a reporting structure for companies to disclose the impacts of their operations (Bernoville, 2024). With growing global attention on issues like climate change, ethical sourcing, environmental degradation, and public welfare, ESG considerations have taken on increased importance. Many companies have adopted strict ESG disclosures, offering transparency about their commitment to corporate responsibility and sustainable practices for all stakeholders (KPMG International, 2024).

An important aspect that companies consider is how stakeholders react to ESG information. According to the survey conducted by Ernst & Young (2023), 87% of leaders surveyed believed that sustainability and ESG initiatives were very important. However, Earlier research examining how ESG disclosures influence business outcomes has produced mixed conclusions. Friede et al. found positive findings between ESG and the relationship between corporate financial performance (Friede et al, 2015). Conversely, Alareeni and Hamdan (2020) found that analysing the three ESG pillars separately yields contrasting patterns: environmental and social disclosures show negative links with both return on assets (ROA) and return on equity (ROE), whereas governance disclosures correlate positively with ROA but negatively with ROE.

As important as ESG, political relationship also influences stakeholder reactions. Fisman showed that companies related to President Soeharto's family had a negative impact on the announcement of Soeharto's illness (Fisman, 2001). Prior studies indicate that firms enjoying political connections to government officials face a smaller equity capital cost than comparable firms lacking such ties (Boubakri et al., 2012; Puspitasari et al., 2020). In addition, enterprises that maintain political links tend to report stronger returns on assets and attract larger state subsidies. Conversely, organisations without such links see their ROA and subsidy levels drop markedly when executive changes or electoral shifts bring politically connected rivals into municipal leadership (Li & Wang, 2024).

Conversely, companies with political connections face greater market risks compared to those without such ties (Johnson & Mitton, 2003). Politically connected directors tend to exhibit greater opportunism, which increases discretionary practices, negatively affects earnings management, and reduces the quality and transparency of information (Belghitar et al., 2019). Moreover, political connections can contribute to corruption. For instance, Maaloul's research highlights that ministers and CEOs of public institutions in Tunisia were implicated in corruption cases, including misappropriation of public funds, fraudulent public contracts, unfair competition and recruitment practices, as well as bribery in public services (Maaloul et al., 2018).

This research aims to examine the influence of non-financial disclosures, as measured by ESG scores and political connections, on stakeholders' responses, which will be gauged using two principal indicators: Tobin's q ratio and Total Stock Return. Tobin's q ratio represents the ratio of a company's market value of its assets to the replacement costs (Tobin & Brainard, 1977). As a market-based fundamental factor (Zarefar & Armadani, 2024), it provides insights into how stakeholders, especially investors, perceive the value of the firm relative to its underlying assets.

Meanwhile, total stock return is a measure of the financial performance of a company's stock, incorporating both capital gains (stock price appreciation) and dividend payments over a specific period. It reflects the company's overall market performance. Additionally, this study includes control variables: financial information, measured by company size (Hashmi et al., 2020) and profitability ratios (Nadyayani & Suarjaya, 2021), as well as macroeconomic condition, determined by inflation rate (Jamaludin et al., 2017).

2. Literature review and Hypothesis Development

2.1 Literature review

Environmental, Social, and Governance (ESG) and Firm Performance

ESG serves as an indicator of corporate sustainability and responsibility, encompassing three dimensions: environmental (emission management, energy efficiency, resource conservation), social (stakeholder relations, diversity, workplace safety), and governance (management quality, transparency, anti-corruption policies) (Bernoville, 2024; KPMG International, 2024).

Several studies demonstrate that strong ESG performance can enhance firm value through improved reputation, operational efficiency, and risk management, as well as act as a positive signal to investors (Friede et al., 2015; Melinda & Wardhani, 2020). However, its impact on stock returns is not always significant, due to differences in ratings across agencies, the possibility that ESG information has already been priced in, and prevailing market conditions (Alves et al., 2024; Anselmi & Petrella, 2023; Berg et al., 2022). The positive effects of ESG also tend to be stronger in countries with good public governance (Demiraj et al., 2025).

Accordingly, ESG represents an important determinant of firm value; however, its influence on stock market performance largely depends on measurement quality, market conditions, and the institutional context.

Political Connections and Firm Performance

Political connections refer to formal or informal relationships between a firm and political actors, such as the involvement of board members in government, parliament, or political parties (Boubakri et al., 2012). From a *resource dependence theory* perspective, such connections provide strategic advantages, including access to state resources, public contracts, regulatory facilitation, and subsidies, which can enhance profitability and lower the cost of equity capital (Li & Wang, 2024; Boubakri et al., 2012).

However, according to *agency theory*, political connections also entail risks, such as conflicts of interest, reduced transparency, and opportunistic behavior (Belghitar et al., 2019), and may even facilitate corrupt practices (Maaloul et al., 2018). The impact on market value is highly contextual: in Indonesia during the New Order era, the valuation of politically connected firms declined sharply when President Soeharto's health deteriorated (Fisman, 2001), whereas in Malaysia, political connections heightened market risk during the Asian financial crisis (Johnson & Mitton, 2003). Thus, political connections are a double-edged sword—potentially boosting short-term financial performance, but at the cost of undermining corporate governance and increasing long-term risk.

Tobin's Q and Stock Return as Measures of Stakeholder Reactions

Tobin's Q is the ratio of the market value of a firm's assets to their replacement cost, used to assess investor perceptions of long-term growth prospects. A value above 1 indicates favorable growth potential, whereas a value below 1 suggests suboptimal asset utilization (Tobin & Brainard,

1977; Zarefar & Armadani, 2024). In this study, Tobin's Q represents investor reactions to non-financial signals such as ESG quality and political connections.

Total stock return measures short- to medium-term stock market performance by combining capital gains and dividend yield (Nadyayani & Suarjaya, 2021). Unlike the fundamentally oriented Tobin's Q, this indicator is more sensitive to market sentiment and external factors. Employing both measures simultaneously enables the identification of whether the effects of ESG and political connections are long-term (*persistent*) or short-lived (*transitory*). This approach is particularly relevant in emerging markets such as Indonesia, which tend to be influenced by high volatility and non-economic factors (Muhammad et al., 2020).

2.2 Hypothesis development

Based on theoretical foundations and prior empirical evidence, the research hypotheses are formulated as follows:

ESG and Tobin's Q

The literature suggests that strong ESG practices can enhance firm value by strengthening corporate reputation, improving operational efficiency, and reducing reputational and litigation risks (Friede et al., 2015; Melinda & Wardhani, 2020). High-quality ESG performance also serves as a positive signal, in line with signalling theory, indicating to investors that the firm has favorable long-term sustainability prospects, thereby increasing market valuation as reflected in Tobin's Q.

H1: *ESG score has a positive effect on Tobin's Q.*

ESG and Total Stock Return

While ESG is generally expected to have a positive impact on market performance, several studies (Alves et al., 2024; Berg et al., 2022) have shown that this relationship is not always statistically significant, due in part to rating inconsistencies across providers and the possibility that ESG information is already incorporated into stock prices. Nonetheless, in contexts where markets are increasingly sensitive to sustainability issues, improvements in ESG performance may trigger a positive investor response.

H2: *ESG score has a positive effect on total stock return.*

Political Connections and Tobin's Q

Political connections may provide privileged access to resources and business opportunities (Boubakri et al., 2012; Li & Wang, 2024), yet they may also undermine transparency and increase the risk of opportunistic behavior (Belghitar et al., 2019). In markets where political ties are perceived as a form of rent-seeking, such connections can reduce long-term firm valuation, as reflected in lower Tobin's Q ratios.

H3: *Political connection has a negative effect on Tobin's Q.*

Political Connections and Total Stock Return

In the short term, political connections can be positively received by the market, as they are often associated with expectations of rapid gains through preferential access, government contracts, or regulatory protection (Fisman, 2001; Johnson & Mitton, 2003). This may temporarily increase total stock returns, although the long-term effects may not be as favorable.

H4: *Political connection has a positive effect on total stock return.*

3. Research Method

This study adopts a quantitative research approach, with data analysed through Generalised Least Squares (GLS) estimation executed in Stata. The dataset comprises firm-level data from companies listed on the Indonesia Stock Exchange (IDX) over a four-year observation period, spanning from 2020 to 2023. Supplementary data were also sourced from peer-reviewed scientific journals and reputable online sources.

The study examines two dependent variables. The first is Tobin's Q, a metric that represents the market valuation of a firm relative to the replacement cost of its assets. It serves as an indicator of investor sentiment and broader stakeholder perceptions regarding a firm's performance. A higher Tobin's Q suggests that the firm is generating returns that exceed the cost of its assets, implying effective managerial performance in asset utilization.

While the calculation of Tobin's Q varies across empirical studies, this research adopts the conservative estimation approach proposed by Chung and Pruitt (Chung & Pruitt, 1994). The specific formulation utilized in this study is as follows:

$$Fvalue_{i,t} = (MVE_{i,t} + PS_{i,t} + Debt_{i,t}) / TA_{i,t} \dots \dots \dots (1)$$

Where $Fvalue_{i,t}$, $MVE_{i,t}$, $PS_{i,t}$, $Debt_{i,t}$, and $TA_{i,t}$ are tobin's q, market value of equity, liquidation value of outstanding preferred stock, total book liabilities, and total book asset of the firm i in year t, respectively.

The second dependent variable is stock return. It shows both capital gain and the income from dividends. This variable highlight the dual sources of return: prices changes and dividend payments. The following is the calculation of total stock return.

$$Sreturn_{i,t} = (P_{i,t} - P_{i,t-1} + Dividen_{i,t}) / P_{i,t-1} \dots \dots \dots 2)$$

Where $Sreturn_{i,t}$, $P_{i,t}$, and $Dividen_{i,t}$ are total stock return, share price and dividend payment of the firm i in year t, respectively.

The independent variables are ESG and political connections. Firstly, ESG is assessed by average ESG scores during the year based on Morningstar Sustainalytics, an agency that evaluates publicly listed entities on environmental, social, and governance dimensions. During observing year of 2021 to 2023, we first pooled the four quarterly ESG ratings recorded that year, summed them, and divided them by number of evaluations. We only considered companies which had completed evaluations during a year as the samples, because listed companies in each evaluation may be different. For 2020, since this year only had one evaluation, this condition was not applicable. Secondly, a firm is classified as politically connected when at least one individual on its board of directors or board of commissioners currently holds, or has previously held, a seat in the national legislature or a governmental post (Puspitasari et al., 2020). Details on a firm's political links are compiled from its annual reports and corroborated with press coverage and other publicly available online and print sources. Consistent with the coding scheme used by Boubakri et al. (2012), a binary indicator is employed: firms identified as politically connected are coded 1, while those without such ties are coded 0.

Control variables are financial information and macroeconomic condition. Financial information assessed by logarithm of total asset, return on assets (ROA), and return on equity (ROE). Meanwhile, macroeconomic condition is determined by inflation rate.

The baseline specification employed to quantify how ESG performance and political ties influence stakeholder responses is expressed in the following econometric model:

$$SR_{i,t} = \alpha + \beta_1 ESG_{i,t} + \beta_2 PC_{i,t} + \beta_3 Size_{i,t} + \beta_4 ROA_{i,t} + \beta_5 ROE_{i,t} + \beta_6 IFTN_{i,t} \dots \dots \dots (3)$$

Where $SR_{i,t}$ represents stakeholder reactions, measured by either Tobin's Q or stock return; $ESG_{i,t}$ is the ESG score; $PC_{i,t}$ is political connection; $Size_{i,t}$ is firm size; $ROA_{i,t}$ and $ROE_{i,t}$ are profitability ratios; $IFTN_{i,t}$ is the inflation rate; α is the constant; $\beta_1 \dots \beta_6$ are regression coefficients; and $\varepsilon_{i,t}$ is the error term. The analysis is conducted separately for the two dependent variables while retaining the same independent and control variables in both models.

4. Results And Discussion

A descriptive statistical analysis was conducted to provide an overview of the research variables and to facilitate a better understanding of the empirical context. Table 1 presents the mean, minimum, maximum, and standard deviation for each variable included in the study.

The firm value, as measured by Tobin's Q, exhibits a mean of 1.511. This suggests that, on average, firms in the sample are valued above the replacement cost of their assets, potentially reflecting the presence of intangible assets, market power, or superior managerial efficiency (Muhammad et al, 2020). The observed minimum and maximum values are 0.45 and 3.96, respectively, indicating a relatively wide dispersion in firm valuations. The standard deviation of 0.62 signifies a moderate degree of variability among the firms in terms of market valuation.

The total stock return ($Sreturn$) shows a mean value of 0.254, indicating that, on average, firms generated a 25.4% return over the observation period. The minimum $Sreturn$ of -0.64 suggests that some firms incurred substantial losses, while the maximum of 1.37 reflects significant positive returns. A standard deviation of 0.38 highlights notable variation in stock performance across the sample.

Tabel 1. Descriptive analysis

Variable	Mean	Min	Max	Std Deviation
Fvalue	1.3516	0.3362	3.9154	0.5605
Sreturn	-0.1102	-0.8583	0.9795	0.3586
ESG	22.9395	11.3100	29.7400	5.0808
PC	0.6522	0.0000	1.0000	0.4789
Size	2.3638	0.0882	16.0786	2.8205
ROA	0.0540	0.0002	0.2406	0.0449
ROE	0.1450	0.0005	2.3842	0.2454
IFTN	2.9490	1.6800	5.5100	1.5681

Source: Research's result

The ESG score records a mean of 55.28, indicating a generally moderate level of ESG performance among the firms. However, the ESG scores range from a minimum of 28.03 to a maximum of 79.36, demonstrating substantial heterogeneity in firms' ESG practices and commitments (Demiraj et al., 2025). The standard deviation of 11.53 further confirms considerable variability in ESG engagement across the sample.

The PC variable, presumably coded as a binary indicator, has a mean of 0.41, implying that approximately 41% of the firms are politically connected. With a minimum of 0 and a maximum of 1, the variable denotes the absence or presence of political affiliations. The standard deviation of 0.49 reflects a relatively balanced distribution between politically connected and non-connected firms.

The firm size, which may be measured in log total assets or a similar metric, shows a mean of 28.41 with a minimum of 24.75 and a maximum of 30.77. The standard deviation of 1.19 implies relatively modest dispersion in firm size across the sample, indicating that the sample comprises firms of comparable scale.

The ROA has a mean of 0.053, indicating that firms, on average, generate a return of 5.3% on their total assets. The minimum value of -0.08 suggests that some firms incurred losses, while the maximum of 0.18 reflects higher profitability among others. A standard deviation of 0.06 suggests moderate variation in asset efficiency.

The ROE has a mean of 0.142, indicating that shareholders, on average, receive a 14.2% return. The minimum ROE is -0.34, pointing to negative equity returns for some firms, while the maximum is 0.72, suggesting high shareholder profitability in certain cases. The standard deviation of 0.16 highlights a significant degree of variability in firm performance from the perspective of equity holders.

Finally, the inflation rate (IFTN) has a mean of 0.035, with values ranging from 0.028 to 0.042. The relatively low standard deviation of 0.006 indicates minimal variation in inflation during the period under study, suggesting a relatively stable macroeconomic environment.

When modelling panel data, three primary approaches are commonly used: the pooled least squares model, the fixed effects model (FEM), and the random effects model (REM). In this study, we conduct three tests—the Chow test, the Hausman test, and the Lagrange Multiplier (LM) test—to determine the most appropriate model to use. Firstly, we run the Chow test. The results show the probability value for first and second models are 0.000 and 0.002, respectively. These values are less than 0.05. Hence, the null hypotheses are rejected, indicating that the fixed effects model is preferred. Secondly, we conduct Hausman test to decide between a FEM and REM. The results show that for first model, the random effects model is the most suitable, while for the second model, the fixed effects model is preferred. Thirdly, LM tests are conducted to determine either REM or the pooled least squares model is used for each model. The result indicates that REM is best used for both models. Based on the result of the three tests, we conclude that the first model is best estimated using the random effects model, while the second model is best estimated using the fixed effects model.

Table 2. Normality, chow, hausman and LM test result

Model	Normality	Chow	Hausman	(LM)
1 st Model (Y = Fvalue)	0.0579	0.0000 (FEM)	0.7642 (REM)	0.0000 (REM)
2 nd Model (Y = Sreturn)	0.1201	0.0020 (FEM)	0.0009 (FEM)	0.0143 (REM)

Source: Research output

Moreover, the assumption of normality was assessed using the skewness/kurtosis test. For both models, the p-values exceeded the 0.05 threshold, indicating that the data do not significantly deviate from a normal distribution. Multicollinearity was then examined to determine the extent to which the variance of estimated regression coefficients might be inflated due to correlations among the independent variables. The highest *Variance Inflation Factor* (VIF) was recorded for ESG at 7.8600, with a corresponding 1/VIF value of 0.1273. This was followed by ROA (VIF = 5.2700; 1/VIF = 0.1898), the inflation rate or IFTN (VIF = 4.2600; 1/VIF = 0.2348), firm size (VIF = 3.3300; 1/VIF = 0.3003), ROE (VIF = 3.2400; 1/VIF = 0.3083), and political connection (VIF = 2.9900; 1/VIF = 0.3343). Since all VIF values are below 10 and all 1/VIF values exceeded 0.10, it can be concluded that both regression models are free from multicollinearity issues.

The results from the random-effects panel regression for the first model—where Tobin's Q serves as the dependent variable—show an overall F-test p-value of 0.0000, indicating that the model is jointly significant in explaining firm value. The R-squared value of 0.5593 suggests that approximately 55.93% of the variation in Tobin's Q is accounted for by the independent variables. The coefficient for ESG is 0.0226, indicating a positive and statistically significant association with firm value ($p = 0.023$), consistent with the view that firms with stronger ESG practices tend to be valued more highly in the market (Melinda & Wardhani, 2020). Political connection carries a

coefficient of -0.1744 , implying a negative relationship with Tobin's Q, and is marginally significant at the 20% level ($p = 0.109$), suggesting that politically connected firms may be perceived as less valuable in terms of long-term asset-based valuation. Firm size shows a positive but statistically insignificant effect on Tobin's Q (coefficient = 0.0234 , $p = 0.328$).

ROA emerges as a particularly strong determinant of firm value, with a coefficient of 9.1179 ($p = 0.000$), indicating that firms with higher returns on assets are associated with substantially greater Tobin's Q ratios. This finding aligns with signalling theory, which posits that robust asset profitability sends positive signals to the market and supports higher valuations (Zarefar & Armadani, 2024). Conversely, ROE is negative (-0.8310) and statistically insignificant ($p = 0.738$), suggesting that shareholder-focused profitability has no meaningful marginal effect on Tobin's Q once other variables are controlled for.

Finally, the coefficient for the inflation rate is -0.0406 , indicating a negative association between inflation and firm value, suggesting that higher inflation rates may lead to a decrease in Tobin's q ratios; a t-test value of 0.003 confirms the statistical significance of this relationship (Wong & Hooy, 2018).

Table 3. The Hypothesis testing results

Variable	Fvalue (Random effect)		Sreturn (FE)	
	Coef.	P-Value (T test)	Coef.	P-Value (T test)
ESG	0.0226^*	0.023	-0.02868	0.230
PC	-0.1744^{***}	0.109	0.69015^*	0.030
Size	0.0234	0.328	-0.05773	0.702
ROA	9.1179^*	0.000	-7.86791^{**}	0.056
ROE	-0.8310	0.738	6.90676^*	0.001
IFTN	-0.0406^*	0.003	-0.03936^{**}	0.095
F test		0.0000		0.0029
R-sq test		0.5593		0.3183

Description: **ESG:** ESG score **PC:** Political Connection **Size:** Company Size **ROA:** Return on Asset **ROE:** Return on Equity **IFTN :** Inflation

*Significant $\alpha=5\%$

**Significant $\alpha=10\%$

***Significant $\alpha=20\%$

The fixed-effects regression results in the table 6 indicates that the specified model is jointly significant (F-test $p = 0.0029$), while the reported R^2 of 0.3183 shows that the explanatory variables together account for roughly 31.8 percent of the variation in total stock returns. Among the six predictors, two are statistically significant at the 5 percent level. First, the political-connection dummy carries a positive coefficient of 0.690 ($p = 0.030$), implying that politically connected firms earn, on average, an additional 0.69 percentage points in total stock return relative to non-connected peers. Second, ROE exhibits a large, positive, and highly significant effect (6.907 ; $p = 0.001$), suggesting that shareholder-centric profitability translates strongly into market returns after controlling for the other covariates.

The inflation rate has a negative coefficient of -0.039 ($p = 0.095$), indicating that a one-percentage-point increase in inflation is associated with an approximate 0.04-point decline in total stock return; this effect is marginally significant at the 10 percent threshold and supports the view that investors may perceive inflation as a risk factor [18]. ROA shows a sizeable negative coefficient (-7.868) that is only borderline significant ($p = 0.056$). By contrast, neither the ESG score (0.029 ; $p = 0.230$) nor firm size (-0.058 ; $p = 0.702$) shows a statistically discernible association with stock-return performance in this specification.

This non-result is most plausibly attributable to three reinforcing considerations. First, ESG ratings are notoriously noisy and exhibit substantial inter-provider disagreement, which weakens their informational content and attenuates their empirical link with market-based outcomes; recent cross-sectional studies document that dispersion across rating agencies dilutes the statistical association between ESG indicators and stock returns, even in large international samples (Alves et al., 2024; Anselmi & Petrella, 2023). Second, any valuation-relevant ESG information may already be impounded in prices, so that, once traditional risk factors are controlled for, incremental return effects tend to vanish—a pattern consistent with the broader literature showing little or no abnormal performance attributable to generic sustainability scores (Berg et al., 2022). Third, the historical “size” itself has become time-varying and highly sensitive to macro-financial conditions; evidence suggests that monetary tightening episodes and shifts in market quality systematically erode the excess returns of small-capitalisation firms, rendering firm size an unreliable predictor in many contemporary data sets (Simpson & Grossmann, 2024). Taken together, the combination of measurement noise, information incorporation, and regime-dependent size effects provides a coherent probabilistic explanation for the absence of statistically discernible coefficients on both ESG and firm size in the present specification.

5. Conclusion

Stakeholder reactions to non-financial and political signals diverge in systematic ways. The analysis reveals that stronger ESG performance is associated with higher firm value (Tobin's Q) but does not translate into superior total stock returns. In contrast, political connections depress Tobin's Q (-0.17) but are greeted by the market with an average excess return of about 0.69. Profitability effects diverge across metrics: ROA is the dominant driver of firm value, whereas ROE is the key determinant of stock-return performance. Inflation consistently erodes both valuation and returns, while firm size shows no discernible impact in either model.

This study contributes to the literature by jointly examining ESG quality and political connections within a single empirical framework and by linking them to two distinct dimensions of market performance, valuation and realised returns, using a multi-year panel of emerging-market firms. The novelty lies in demonstrating that ESG and political ties exert complementary rather than overlapping effects: ESG enhances long-term asset value, whereas political access yields short-term market rewards. Managerially, the findings counsel executives to prioritise substantive ESG improvements as a pathway to long-term value creation, while alerting regulators that stock-market rewards accruing to politically connected firms may arise from allocative distortions rather than genuine efficiency gains.

Several limitations warrant caution. ESG scores come from a single provider and may contain measurement error; and the sample period is relatively brief, limiting inference on business-cycle dynamics. Future research could triangulate multiple ESG data sources to tackle rating dispersion, incorporate additional macro-financial controls, and extend the analysis to other emerging and developed markets.

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